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SENSITIVE

FOR A/USTR REGINA VARGO FROM AMBASSADOR STRUBLE

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SUBJECT: ANDEAN FTA: LIMA ROUND SCENESETTER FOR A/USTR VARGO

¶11. (SBU) We very much look forward to your April 17-22 visit to Lima for the ninth round of the U.S.-Andean Free Trade Agreement (FTA) negotiations. Peruvian public support for the FTA, at 68 percent, continues to be the highest in the region and the government remains committed to concluding negotiations by July 2005. In addition to your busy negotiations schedule, we have arranged opportunities for you to engage in key outreach activities through a site visit to a local apparel exporter, a meeting with Members of Peru's Congress, breakfast at the Ambassador's residence with English speaking media leaders, and a lunch with Peruvian Ministers (also at the residence). We have also requested meetings with President Alejandro Toledo and Trade Minister Ferrero. The persistence of several commercial disputes between U.S. companies and the Peruvian Government remains a top concern. You will have ample opportunities to push for progress during your bilateral meetings with the Peruvians.

Political Scene

¶12. (SBU) President Alejandro Toledo is approaching the last year of his term as a lame duck, with his popularity mired in the low-teens. Peru's strong economic growth is beginning to trickle down to the poorest classes, but President is getting little credit for this from the population. The GOP's strength is visibly declining, as the governing coalition composed of his Peru Possible party and the Independent Moralizing Front is fraying and fringe Peru Possible legislators are quitting the party to further their reelection prospects. A minor Cabinet reshuffle in February did not generate enthusiasm, and major changes are expected by July, including the possible replacement of Prime Minister Carlos Ferrero, who survived two censure motions over the past six months. Rural unrest continues to bedevil the regime, including violent anti-mining protests, demonstrations by small agricultural producers seeking subsidies, and cocalero blockades. Toledo is further distracted by ongoing congressional and judicial investigations into allegations that his party engaged in the massive falsification of signatures in order to register for the 2000 elections.

¶13. (SBU) Despite its weaknesses and challenges, the Toledo Government is not facing a serious threat to its survival. With presidential and congressional elections a year away, the major opposition parties are interested in maintaining institutional stability to ensure a free and fair election and a smooth transition to the next administration, which they hope to lead. Consequently, they no longer show an interest in terminating Toledo's presidency, and, in fact, have tempered investigation into alleged party registration involving the President and his party. Instead, political leaders and their parties are focused on reaching out to economic and social sectors for support, while warily exploring alliance options with each other.

¶14. (SBU) President Toledo has two goals for the remainder of his term. First, he wants to cement his legacy by finalizing international agreements and projects that will serve as the foundation for Peru's future development, such as the Free Trade Agreement with the U.S., the southern highway connection to Brazil, and the Camisea liquefied natural gas plant. The opposition political parties, who stand to benefit from these accomplishments if they win office in 2006, support these objectives in principle though they may differ on certain details. Second, he wants to ensure that Peru Possible retains a sizable block of legislators in the next Congress to maintain his political influence, block retaliation against his government, and provide a base for a possible 2011 candidacy. The GOP's chief initiative this year, a conditional cash transfer program that would distribute \$30/month to Peru's poorest families, is widely criticized as an election-year popularity ploy aimed at boosting Peru Possible's chances, and opposition parties are considering ways in which to block that proposal.

Strong Macroeconomics, but Challenges Remain

¶16. (U) Peru's economy is one of the most dynamic in Latin

America. 2004 GDP reached \$67 billion, an increase of 5.1 percent. Growth was driven by exports, construction, mining, investment, and domestic demand. Peruvian exports, propelled by high mineral prices, ATPDEA benefits and the completion of the Camisea gas project, swelled to over \$12 billion in 2004, up 39 percent in dollar terms from 2003. U.S. exports to Peru increased 27 percent during the same period, to reach \$1.8 billion. The resulting trade surplus of \$2.6 billion drove up reserves to a record \$12.6 billion, and caused the currency to appreciate 5.5 percent against the dollar by the end of the year.

¶7. (U) Peru's major trading partners are the U.S., EU, China, Chile and Japan. In 2004, 29 percent of exports went to the U.S. and 20 percent of imports came from the United States. Leading exports include gold, copper, fishmeal, petroleum, zinc, textiles, apparel, asparagus and coffee. Imports include machinery, vehicles, processed food, petroleum and steel. The registered stock of foreign direct investment (FDI) is \$12.9 billion, with the U.S., Spain and Britain the leading investors. FDI is concentrated in mining, electricity, telecom and finance.

¶8. (U) Despite Peru's macroeconomic success, major challenges remain. The GOP must reduce poverty of 52 percent (under \$58/month) and extreme poverty of 24 percent (under \$32/month). Wealth and economic activity are overly concentrated in Lima and other major cities. Unemployment and underemployment levels total 56 percent nationwide and over 60 percent of the economy is informal. Growth is barely strong enough to generate employment faster than new entrants come into the labor force. The government lacks revenues for adequate social investment. Boosting long-term growth and reducing poverty will require strengthening the judiciary and other institutions, reducing corruption and completing other reforms to improve the investment climate.

Positive Local View on the FTA

¶9. (SBU) You will find during your outreach activities that most Peruvians, including Congressmen, have a favorable view of an FTA with the United States; this perspective is reflected in editorial coverage by the print and media broadcast. Questions as to the ability of Peruvian agriculture to compete effectively continue to be voiced, however, by some commentators and industry representatives, while press concerns expressed early in the negotiations regarding the local impact of proposed IPR protections have abated. Minister Ferrero's comments after the Washington mini-round that the time had arrived to play the "coca" card did resonate with some editorialists, though little has been said or written on the subject in the last few weeks.

¶10. (SBU) A January 2005 study of the general population commissioned by USAID found that 68 percent of those interviewed felt that Peru would benefit from the FTA. Increased employment and economic stability were the mostly commonly cited benefits. However, lack of information and disinformation is common. Nearly 52 percent claim that they are not informed at all regarding the FTA negotiations. In addition, 55 percent felt that the U.S. would benefit more from an FTA than would Peru; 31 percent aid the latter would be favored. The study also showed that 84 percent could not name members of the Peruvian negotiating team. Only 23 percent of those polled indicated that they have confidence in the Peruvian delegation, with 44 percent lacking confidence. During your visit, you should take the opportunity to publicly praise the professionalism of the Peruvian FTA team.

Outreach Opportunities

¶11. (SBU) Your outreach activities begin with a visit to a textile and apparel producer on Monday, April 18. You will be taken on a tour of the factory, accompanied by Trade Minister Alfredo Ferrero and Agricultural Minister Manuel Manrique. The press will observe and you should expect to take some questions with the Trade Minister.

¶12. (SBU) On Tuesday, April 19, you will be attending a breakfast at the Ambassador's residence with English-speaking media directors. This meeting will be helpful to put into perspective controversial topics such as agriculture and IPR and to reiterate how Peru has benefited from ATPA and ATPDEA.

¶13. (SBU) Later that day, you will be participating in an AmCham lunch at the Marriott Hotel, along with other chief negotiators: Hernando Jose Gomez, Christian Espinoza Canizales and Pablo de la Flor.

¶14. (SBU) In the evening of April 19, you will hold a private meeting with members of the Peruvian Congress at the Sheraton Hotel. No press will be allowed inside the meeting, but you might be asked questions by the media upon your departure. We expect the questions and comments to focus on agriculture,

IPR, and used clothing.

¶15. (SBU) On April 20, you will be having lunch at the Ambassador's residence with several key Peruvian Ministers, including the Ministers of Trade, Finance, Agriculture, Labor, Health, and Production. You will have an opportunity to discuss openly Peru's expectations for the FTA and the realities behind a U.S. Congressional approval of said agreement. This is also an important opportunity to underline the need for Peru to develop now a political strategy to sell the FTA. In that connection, it would be useful to observe that public infighting about FTA positions by cabinet members damages the GOP's own position with its public.

¶16. (SBU) We have requested a meeting for you with President Alejandro Toledo, as well as a separate meeting with Trade Minister Alfredo Ferrero. We are awaiting confirmation.

ADVANCING THE TRADE AGENDA

¶17. (SBU) Your presence and outreach activities should bolster further understanding of the U.S.-Andean FTA and the remaining processes. The meeting with key ministers will be instrumental in establishing realistic expectations among the new cabinet ministers, as well as in explaining how we reach closure on the difficult issues, such as agriculture and IPR. We expect the session with President Toledo should help focus him on GOP plans to move the trade deal through his Congress as well as reiterate the need to resolve the pending commercial disputes.

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